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In the Supreme Court of the United States

OCTOBER TERM, 1956

No. 393

GEORGE BERNSTEIN, et al., PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINION BELOW

The opinion of the Court of Appeals (Pet. App. 1a-24a) is reported at 234 F. 2d 475.

JURISDICTION

The judgment of the Court of Appeals was entered on May 31, 1956. (Pet. App. 1a) A petition for rehearing was denied on August 7, 1956. The petition for certiorari was filed on September 6, 1956. The jurisdiction of this Court is invoked under 28 U.S.C., Section 1254(1).

QUESTIONS PRESENTED

1. Whether funds, representing unrecorded and unreported receipts, diverted by petitioners from a corporation of which they were the sole stockholders are taxable to them as dividend income.

2. Whether, in the light of the charge as a whole, it was prejudicial error for the court to include in the instructions on intent the language that "the law presumes that every man intends the legitimate consequences of his own acts."

3. Whether, in the absence of a request to do so, the court's failure to excuse the jury while petitioners' counsel stated his objections to the charge, was prejudicial error.

STATUTE AND RULE INVOLVED

Internal Revenue Code of 1939:

SEC. 145. PENALTIES.

* * * * *

(b) *Failure to Collect and Pay Over Tax, or Attempt to Defeat or Evade Tax.*—Any person required under this chapter to collect, account for, and pay over any tax imposed by this chapter, who willfully fails to collect or truthfully account for and pay over such tax, and any person who willfully attempts in any manner to evade or defeat any tax imposed by this chapter or the payment thereof, shall, in addition to other penalties provided by law, be guilty of a felony and, upon conviction thereof, be fined not more than $10,000, or imprisoned for

not more than five years, or both, together with the costs of prosecution.

* * * * *

(26 U.S.C. 1952 ed., Sec. 145(b).)

Federal Rules of Criminal Procedure:

Rule 30. INSTRUCTIONS.

At the close of the evidence or at such earlier time during the trial as the court reasonably directs, any party may file written requests that the court instruct the jury on the law as set forth in the requests. At the same time copies of such requests shall be furnished to adverse parties. The court shall inform counsel of its proposed action upon the requests prior to their arguments to the jury, but the court shall instruct the jury after the arguments are completed. No party may assign as error any portion of the charge or omission therefrom unless he objects thereto before the jury retires to consider its verdict, stating distinctly the matter to which he objects and the grounds of his objection. Opportunity shall be given to make the objection out of the hearing of the jury.

STATEMENT

On January 27, 1954, seven indictments were returned in the United States District Court for the Southern District of Florida charging petitioners with attempted evasion of their individual income taxes, and of the income taxes of a corporation of which they were the sole stockholders, for the years 1947, 1948 and 1949, and with a conspiracy to evade the corporate taxes. The

reported and the corrected net income and tax liability as alleged in the several indictments were as follows (R. 1-3, 40-42, 56-58, 73-76, 92-95, 117-119, 130-132):

		Reported		Corrected	
Year	Taxpayer	Income	Tax	Income	Tax
1947	Bernstein	$17,783	$ 4,619	$32,869	$12,776
1948	Bernstein	4,989	230	13,430	1,857
1949	Bernstein	932	-00-	4,751	191
1947	Scherer	14,371	3,790	29,290	11,551
1948	Scherer	9,351	1,473	17,744	3,572
1949	Scherer	4,742	588	9,089	1,416
1947	Hammerman	11,865	3,000	26,951	10,469
1948	Hammerman	4,256	507	12,696	2,238
1949	Hammerman	1,863	110	6,210	859
1947	Hodesblatt	16,400	4,448	31,486	12,551
1948	Hodesblatt	12,876	2,142	21,317	4,461
1949	Hodesblatt	5,207	565	9,132	1,309
Oct. 31					
1947	Selray Corp.	18,010	4,042	75,424	28,661
1948	Selray Corp.	15,177	3,390	51,404	19,533
1949	Selray Corp.	(2,140)	-00-	21,607	4,901

After a jury trial, petitioners were found guilty as charged. (R. 22, 54, 70, 80-83, 107-110, 127, 145.) On December 10, 1954 each of the petitioners was sentenced to imprisonment for one year on each count on which he was convicted the sentences to run concurrently, and, with the exception of Gersch, each was fined varying amounts. (R. 30-32, 55-56, 71-72, 83-91, 110-117, 128-129, 145-147.) The Court of Appeals unanimously affirmed (Pet. App. 1a-24a.)

The evidence to support the verdict may be summarized as follows.

Petitioners Bernstein, Hammerman, Scherer and Hodesblatt, also known as Hodes, were the officers, directors and sole and equal stockholders of the Selray Corporation which leased and operated a beachfront hotel, known as the Surfside, in Miami Beach, Florida. (R. 222-225.) Petitioner Gersch, an accountant, was

employed by the officer-stockholders to prepare false records in furtherance of a plan to defeat and evade the income tax of the Selray Corporation. (R. 542, 549-550.)

The corporation's books were kept and its tax returns were filed on an accrual basis and for fiscal years ending October 31. (R. 160-161.) Eileen Jensen was employed as bookkeeper and office manager. Insofar as pertinent, the underlying records of income from the operation of the hotel consisted of "daily transcripts" which reflected all charges to guests; "front office" cash sheets on which were entered receipts from and expenditures for guests; and the duplicate copies of guest bills which the hotel retained and which also reflected all charges to guests. The daily transcript and cash sheets were prepared by the desk clerks and were audited daily by Jensen who made the postings to the general ledger from which the tax returns were prepared. (R. 521-541.)

In the early part of November 1946 (R. 544-545), Hodesblatt, who was president of the corporation, told Jensen that "he was interested in doing something to see if they could hold out some income to keep the tax down" and that she should "think about it, and we will discuss this later" (R. 546). Shortly thereafter (R. 547), Hodesblatt informed her that "they were going ahead with the plan" and that "they were going to import a man to re-write the transcript" (R. 548). About the same time, Scherer told her that "he had a very good friend that they were going to bring in to do this work who was fully qualified, and was a crackerjack at figures". (R. 549.) Later the same month, Scherer introduced Jensen to the petitioner Gersch and in-

formed her that "Mr. Gersch was the man who was going to do the re-write job" and that Gersch would explain to her the details of the plan to omit income from the corporate books and tax returns. (R. 550, 553, 554.) Jensen testified that she and Gersch told Scherer at the time that "it was wrong to do this, and be sure he knew what he was doing" to which Scherer replied that "this was what his partners wanted to do, and they would do it whether it was done here or whether they sent the records to New York to have the re-write job done". (R. 551.)

About December 9, 1946, Gersch came to Jensen's office in the hotel, showed her the first daily transcript sheets which he had "re-written", and explained the details of the scheme designed to evade the corporation's taxes. The plan was as follows: The original daily transcript prepared by the night clerk was to be used by Gersch in preparing a second transcript in which he would omit the income attributable to a selected number of rooms. The front office cash sheet was to be re-written or altered in order to erase any record of the receipt of the omitted income. Jensen was to audit daily the original transcript and cash sheet as had been her practice. However, she was to post to the general ledger the amounts of room revenue and cash receipts as reflected in the false transcripts and altered cash sheets. She was to deposit only the amount of cash receipts as shown by the altered records. The difference, corresponding in amount to the omitted income, was to be segregated by her in an envelope and placed in a hotel lock box until such time as the officers called for it. (R. 553-566.)

The scheme to evade taxes was carried out during a part of each of the corporation's fiscal years ended in

1947, 1948 and 1949. The periods involved were from December 1946, through April 1947; from November 1947, through April 1948; and from February through April 1949. (R. 558-560, 599-600, 618, 637.) Gersch participated in the scheme as planned during the periods in 1946, 1947, and 1948; he did not participate in 1949. (R. 600, 618-619.) In February 1949, Bernstein and Scherer requested Jensen "to hold out approximately twenty-five thousand dollars of 1949's income." (R. 618.) She did so by falsifying footings on the daily transcripts and cash sheets and posting the false figures to the general ledger. A set of false records was not prepared for the three month period in 1949. (R. 618-620.)

The unrecorded and unreported receipts thus diverted from the corporation were turned over by Jensen to the officer-stockholders, periodically, at their request, at which times Jensen obtained from them receipts for the money. The Government introduced in evidence receipts for these funds signed by three of the petitioners, Bernstein, Scherer and Hodesblatt. (R. 563-631, Ex. 47-51.) Jensen delivered the first envelopes containing the withheld receipts to Hodesblatt in February 1947. (R. 566.) About ten minutes after delivering the envelopes, she was called by Hodesblatt to a small room in the hotel which was used by the officers. There she found the four officers seated around a table with a pile of cash in front of each. Upon entering Hodesblatt told her that "the money he had there did not add up to what he had signed for." She then looked around the table and found an unopened envelope which contained the difference. (R. 582-584.) On another occasion when she was asked by Scherer for $12,000 of

the withheld funds, she prepared four envelopes with $3,000 in each. (R. 623-631.)

At the direction of Bernstein, Hodesblatt and Scherer, Jensen destroyed substantially all of the true daily transcripts and cash sheets for the periods involved together with certain other hotel records before she terminated her employment with the corporation. (R. 637, 642-646, 736.) The duplicate copies of the guest bills which reflected all charges to guests were not destroyed. These together with other books and records of the corporation were turned over to the agents by the officers in the course of the investigation. (R. 735-736.)

The agents determined the correct amounts of revenue received by the corporation during the months in which the scheme to evade taxes was in operation by auditing the duplicate copies of the guest bills and comparing the resultant figures with the amounts entered in the appropriate revenue account in the general ledger. The amounts of revenue omitted from the books and tax returns for the fiscal years ended in 1947, 1948 and 1949 were $57,880, $36,227, and $24,078, respectively, or a total of more than $118,000. After taking into account the correct tax liability of the corporation, computed after adding the omitted income to gross receipts as reported, the agents made a computation which showed earnings or profits available for distribution as dividends in each of the fiscal years in the following amounts which total in excess of $111,000: 1947, $57,880; 1948, $36,227; 1949, $17,384. The amounts diverted from the corporation by the officer-stockholders in the calendar years 1947, 1948 and 1949, no part of which was reported by them in their individual returns, were as follows: 1947, $68,135; 1948, $35,542;

1949, $24,683. The available earnings or profits of the corporation during the calendar years 1947, 1948 and 1949 were sufficient to cover dividend distributions in the amounts of $60,347, $33,761, and $17,384, respectively. One fourth of the latter amounts was included in the unreported income alleged in the indictments charging each of the four officer-stockholders with attempted evasion of individual income tax, and these sums were identified by the Government in its bills of particulars as dividend income from the Selray corporation. (R. 12, 67, 124, 141, 735-905; Ex. 1, 25, 47-51, 64-70.)

At the trial, petitioners made a proffer of evidence to show that during the fiscal years involved the corporation had no earnings or profits available for distribution as dividends, and that, consequently, the diverted funds could not constitute dividend income to the officer-stockholders as alleged in the bills of particulars. Through the testimony of an attorney who had represented petitioners at a conference with representatives of the Internal Revenue Service, an exhibit (Pet. App. 1b) was offered which purported to show a calculation by the Service of proposed deficiencies and civil penalties against the corporation for the years involved herein. (R. 1056-1078.) A second exhibit was offered (Pet. App. 2b-5b) through the testimony of an accountant which purported to show that after accruing the proposed deficiencies and civil penalties, with interest thereon to the date of trial, the corporation had no earnings or profits available for distribution as dividends in any of the years in question. (R. 1194-1209.) The proffered evidence was excluded by the court as immaterial and irrelevant. (R. 1070, 1078, 1205-1206, 1209-1210.)

The court instructed the jury on the element of wilfulness, in part, as follows (R. 1244-1245):

> Now intent may be ascertained from all the facts in evidence and the inferences that reasonable men might naturally draw from the evidence. The law presumes that every man intends the legitimate consequences of his own acts, and a man is charged with knowledge of that which naturally and normally from all the evidence flows or results from his acts normally done or performed. There must be a union or joint operation of act and intent. It is not possible to look into the mind of a man and see what its workings are, or to bring a photograph of the mind of a man and exhibit it to the jury, so as to determine clearly and absolutely what the workings of a human being's mind are, and from necessity, intent with which an act is done is to be drawn or determined from all the surrounding circumstances.

After completing the principal portions of the charge to the jury, the court stated to counsel (R. 1247): "I think I have covered each of the instructions you gentlemen have submitted and we agreed on." Petitioners' counsel then stated: "If the Court please, I'd like to be heard on certain matters." The court asked if there were any more instructions and a defense request to give "Instruction No. 8" was granted. Thereafter petitioners' counsel stated: "I'd like to take exception to particular items" and the court replied (R. 1248): "You may have exception to all instructions that the Court gave." During the colloquy which followed (R. 1248-50) petitioners' counsel made no request to have the

jury excused while the court entertained exceptions or to approach the bench. Nor was the court's attention directed to Rule 30 (supra, p. 3).

After retiring to consider its verdict, the jury was twice recalled to the courtroom for additional instructions, on the second occasion at the instance of petitioners' counsel. (R. 1250-1257.)

ARGUMENT

1. The four petitioner-stockholders contend (Pet. 12-20) that the Government has failed to prove that the unrecorded and unreported receipts which they diverted from the corporation are taxable to them as dividend income, as alleged in the bills of particulars, since the Government failed to establish that the corporation had earnings or profits available for distribution as dividends. This contention ignores the facts of record and is without merit. It is clear from the record that in computing the amounts of unreported income identified in the bills of particulars as dividend income, the Government was guided by the extent of the corporate earnings or profits available for distribution as dividends in each of the fiscal years involved. Moreover, in computing the available earnings for each year, the Government took into account and accrued the additional taxes attributable to the unreported income. As a result, although the proof showed that during the years involved the petitioners had diverted corporate receipts aggregating in excess of $118,000, the amounts of unreported dividend income alleged in the bills of particulars totaled only $111,000, *supra*, pp. 8-9. All the items entering into the Government's computation of unreported dividend income are contained in the ex-

hibits in evidence.[1] (Ex. 1, 64, 68-70.) In short the diverted funds were taxed to the petitioner-stockholders as constructive dividends to the extent of the corporation's available earnings or profits as shown by the evidence. See *Currier* v. *United States,* 166 F. 2d 346 (C. A. 1st); *United States* v. *Augustine,* 185 F. 2d 407 (C. A. 3d), on rehearing remanded on other grounds, 189 F. 2d 587.

Petitioners' assertion (Pet. 17) that the trial court was of the opinion that no earned surplus need be shown is not an accurate reflection of the record (R. 850-954, 896-905, 912-919) which shows that the court had a correct appreciation of the government's theory of the case. Nor did the trial court err, as petitioners contend (Pet. 16-19), in excluding as immaterial and irrelevant the evidence proffered by petitioners which purported to show that the corporation had no earnings available for distribution (R. 1056-1078, 1194-1209). The excluded evidence was offered by petitioners on the theory that in computing earnings or profits for a corporation on an accrual basis, the Government is required to accrue as of the end of each fiscal year amounts which petitioners claim are the deficiencies and civil penalties which the Commissioner of Internal Revenue *proposes* to assess against the corporation, with interest thereon to the date of trial. This novel proposition is without support in authority. Petitioners' reliance upon *Stein*

[1] Petitioners objected to the offer in evidence by the Government of an exhibit (Government's Exhibit 71 for identification) summarizing the data in the various other exhibits relating to the computation, and the court reserved ruling on the offer (R. 854). The Government did not thereafter press for its introduction since the underlying data was already in evidence. Petitioners' statement (Pet. 17) that the court "refused to admit" the exhibit is therefore inaccurate.

v. *Commissioner*, 25 T. C. 940, is misplaced. The *Stein* case was a proceeding before the Tax Court for a redetermination of deficiencies and civil fraud penalties which had been determined by the Commissioner against a closely held corporation and its stockholders. Suffice it to note that here there has been no determination by the Commissioner of the civil tax liability of the corporation for any of the years involved. As the court below noted (Pet. App. 11a-12a), what deficiencies and civil penalties, if any, will ultimately be determined against the corporation is a matter of speculation. It had no place in the trial of these criminal charges, and the court properly excluded the proffered evidence.

Furthermore, even if the rationale of the *Stein* case were to be applied here, it would not aid petitioners in view of the concurrent sentences imposed by the court for the various offenses of which petitioners stand convicted.[2] The decision would not affect their conviction under count one of the indictments charging attempted evasion of their individual income taxes in 1947;[3] nor would it have any bearing on their conviction of the charges of conspiracy and of attempted evasion of the corporation's income taxes. As petitioners recognized (Pet. 13-16) the contention predicated on the *Stein* case relates only to the computation of individual taxes.

---

[2] The sentences imposed for the various offenses are to run concurrently with each other and with the sentences imposed for the conspiracy offense.

[3] In *Stein* the Tax Court held that in the case of an accrual basis corporation, the addition to a deficiency for fraud accrues and is deductible in determining earnings or profits, not at the end of the taxable year to which it applies but in the year in which the fraudulent return was filed. Consequently, even under the *Stein* decision, the Government's computation of earnings or profits and dividend income for the first year (1947) would not be disturbed.

2. There is likewise no merit in petitioners' contention (Pet. 27-32) that it was prejudicial error for the court to include in the instructions on intent the language that "the law presumes that every man intends the legitimate consequences of his own acts." The charge on intent (R. 1232, 1239-1241, 1244-1245), as the court below noted (Pet. 15a, 20a), was "unusually full and complete" and gave the jury "the correct legal standard to apply." Under these circumstances, the mere use of the challenged phrase does not constitute reversible error. *Imholte* v. *United States,* 226 F. 2d 585 (C.A. 8th); *Banks* v. *United States,* 223 F. 2d 884 (C. A. 8th); *Legatos* v. *United States,* 222 F. 2d 678 (C. A. 9th); *Bateman* v. *United States,* 212 F. 2d 61 (C. A. 9th). This is particularly true where, as here, it is readily apparent that the challenged language could not have misled the jury to the prejudice of petitioners. Here, the question of wilfulness was largely resolved for the jury if the jury believed, as it evidently did, the testimony of the witness Jensen which clearly implicated petitioners in a conspiracy to evade tax.

The decision below is not, as petitioners assert (Pet. 28-31), in conflict with the decisions of this Court in *Bollenbach* v. *United States,* 326 U.S. 607, and *Morissette* v. *United States,* 342 U.S. 246. Nor is it in conflict with the decisions of the Courts of Appeals in *Wardlaw* v. *United States,* 203 F. 2d 884 (C. A. 5th); *Frank* v. *United States,* 220 F. 2d 559 (C. A. 10th); and *McFarland* v. *United States,* 174 F. 2d 538 (C. A. D. C.). In *Bollenbach,* a prosecution for conspiracy to violate the National Stolen Property Act, this Court struck down a charge (326 U.S. 609) that "possession of stolen property * * * raises a presumption that the

possessor was the thief and transported [the] stolen property in interstate commerce." In the *Morissette* case, the charge condemned by this Court withdrew from the jury the issue of specific intent and was tantamount to a directed verdict of guilty. There was no such vice in the charge in the case at bar. Nor did the challenged language deprive petitioners of their defense, as was true in the *Wardlaw* case. The *Frank* and *McFarland* cases actually support the government's position in that in each instance the court recognized that if the charge as a whole correctly stated the law, the incorrectness of one phrase standing alone ordinarily does not constitute reversible error.

3. Finally, petitioners contend (Pet. 20-27) that, contrary to the provisions of Rule 30, Federal Rules of Criminal Procedure, *supra,* they were denied the opportunity to state fully their objections to the charge out of the hearing of the jury. The contention is without merit. This is not a case in which the court refused to entertain objections to the charge out of the presence of the jury. Petitioners concede (Pet. 21) that counsel did not specifically request an opportunity to state objections to the charge out of the hearing of the jury (R. 1247-1250). This being so they can hardly be heard to complain that the opportunity was denied them.

Petitioners argue, however, that the court should have recognized the colloquy which followed the charge (R. 1247-1250) as a request by counsel to state his exceptions out of the hearing of the jury as contemplated by Rule 30, although counsel did not invite the court's attention to the rule now relied on. The short answer to this argument is that even if counsel's remarks

were to be construed as a request to the court to hear exceptions to the charge out of the presence of the jury, there is no showing that petitioners were prejudiced by the court's failure to regard them as such. In view of the fact that the jury was twice recalled for further instructions, it is apparent, as the court below noted (Pet. App. 14a), that petitioners' counsel had ample opportunity to state any objections to the charge out of the presence of the jury and to request the court to give supplemental instructions in accordance with his view of the applicable law. In fact the record shows (R. 1252-1257) that on the occasion of the second recall of the jury supplemental instructions were given by the court at the instance of petitioners' counsel. Compare, *Schaffer* v. *United States*, 221 F. 2d 17 (C.A. 5th); *United States* v. *Hall*, 200 F. 2d 957 (C.A. 2d). Consequently, even if there was a deviation here from strict compliance with the rule, the error, if any, was harmless. See *United States* v. *Titus*, 221 F. 2d 571 (C.A. 2d); *United States* v. *Hall*, *supra*; *Steinberg* v. *United States*, 162 F. 2d 120 (C.A. 5th), certiorari denied, 332 U.S. 808.

Contrary to petitioners' assertions (Pet. 21-27), the decision of the court below is not in conflict with the decision of this Court in *Escoe* v. *Zerbst*, 295 U.S. 490, which is not in point, nor with the decisions of the Court of Appeals for the Fourth Circuit and the District of Columbia Circuit in *Lovely* v. *United States*, 169 F. 2d 386 (C.A. 4th) and *Butler* v. *United States*, 188 F. 2d 24 (C.A. D.C.). In *Escoe* v. *Zerbst*, *supra*, this Court construed a statute governing the procedure for revocation of parole. In the *Lovely* case, although the court refused to hear exceptions to the charge out of the presence of the jury, the decision was based on other

grounds and the language relied upon by petitioners was *dicta*. In the *Butler* case, the court refused to allow counsel to state for the record his objections to the manner in which the charge was delivered, specifically, the gesticulations and facial expressions of the judge. Here, as already noted, there was no refusal by the court to hear, nor lack of opportunity for counsel to state exceptions to the charge out of the presence of the jury.

CONCLUSION

For the reasons stated, the petition for certiorari should be denied.

Respectfully submitted,

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